

ECONOMIC FORECAST

Review of FY 2008

The national economy continued to grow at below-trend rates in FY 2008. Consumer spending increased moderately, driven by employment and personal income growth. The national economy added jobs in FY 2008, with solid gains in the services sector offsetting losses in the construction and financial sectors. Despite posting growth throughout FY 2008, the weight of evidence suggested that the economy had slipped into a mild recession in the latter half of the fiscal year. The downturn had spread beyond the housing market, as tight credit and soaring commodity prices reduced spending.

The Virginia economy weakened more than expected over the course of FY 2008. The slowdown in housing and higher energy prices had a significant impact on economic growth during the second half of the fiscal year. As a result, growth in total nonagricultural employment and income were weaker than projected. As is typical in Virginia, the services sector drove the majority of growth. The employment sectors most-closely related to the housing industry, construction and financial activities, posted substantial job losses.

National economic growth moderated in FY 2008

The U.S. economy slowed in FY 2008, with the housing slowdown spreading to other sectors of the economy.

Growth in U.S. Gross Domestic Product was below-trend in FY 2008. The value of all goods and services produced within the U.S., adjusted for inflation, grew at 2.4 percent in FY 2008. Growth in total personal income was 5.3 percent, while wages and salaries increased by 4.6 percent.

Consumer spending slowed. Consumer spending grew by 1.9 percent in FY 2008.

Employment growth decelerated in FY 2008. Major drivers were leisure and hospitality services, professional and business services, and education and health services.



The Federal Reserve cut the federal funds rate as the economy slowed in the second half of FY 2008. The federal funds rate target was reduced by 75 basis points in an emergency January meeting. Further cuts lowered the rate to 2.00 by the end of the fiscal year.

US Economy Falls into Recession

	Actual	Forecast	
	2008	2009	2010
Real GDP	2.4%	-0.4%	0.1%
Total Employment*	0.7%	-1.0%	-0.9%
Unemployment	4.9%	6.8%	8.1%
CPI	3.7%	1.6%	0.2%

* Total nonagricultural employment. Figures represent percent change over previous year, except the unemployment rate, which is a percentage. Data based on the November 2008 Global Insight standard forecast. Source: Department of Taxation

In Virginia, the economy trended towards slower growth.

Employment growth was weaker than anticipated in FY 2008. Year-over-year job growth of 0.9 percent was slightly below the annual forecast of 1.1 percent growth. Total nonagricultural employment increased by 33,900 jobs -- 7,600 fewer jobs than anticipated in the official forecast -- after increasing by 64,400 on average over the prior four fiscal years. As is typical, the services sector drove the majority of growth.

Here is a look at regional employment in Virginia during FY 2008:

Northern Virginia

In Northern Virginia, which represents 35 percent of all jobs in the state, total employment increased by 1.3 percent (17,100 jobs) -- 50 percent of total state gains for the year. The housing slowdown hit Northern Virginia especially hard in FY 2008, with the construction and financial activities sectors shedding 9,100 jobs for the year. The housing-related weakness was offset by continued gains in professional and business services employment. The area continued to benefit from its proximity to Washington, D.C., with a substantial amount of federal government contract funds flowing to area companies.

Richmond/Petersburg

Employment in the Richmond-Petersburg Metropolitan Statistical Area (MSA) (17 percent of state employment) increased 1.0 percent (6,400 jobs) in FY 2008. Gains were centered in the education and health services and trade, transportation, and utilities sectors. Despite the slowdown in housing, construction employment actually increased slightly for the year, the only region in the state to experience an increase. The financial activities sector shed 1,100 jobs during the year, the largest sector decline.

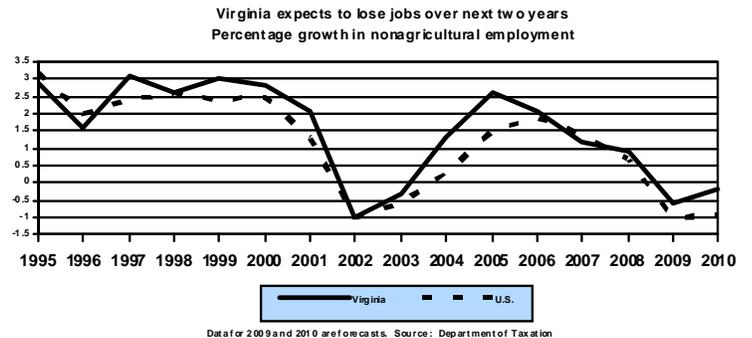
Norfolk/ Virginia Beach/ Newport News

The Norfolk-Virginia Beach-Newport News MSA (20 percent of state employment) experienced employment growth of 0.5 percent in FY 2008. The region had a gain of 4,000 jobs, with losses in manufacturing (down 2,000 jobs) and construction (down 1,700 jobs) offset by gains in the service sector. The continued deployment of many of the military personnel situated in the area remained a drag on growth. The tourism industry, long a staple of the area economy, added only 500 jobs in FY 2008, one-fifth of the amount added on average over the prior three fiscal years.

Balance of the state

Outside of the three major metro areas, the remainder of the state (28 percent of state employment) added 6,400 jobs in FY 2008, growth of 0.6 percent. Gains in education and

health services were partially offset by continued declines in manufacturing employment, primarily in Southwest Virginia. Housing-related employment declined by 2,100 jobs.

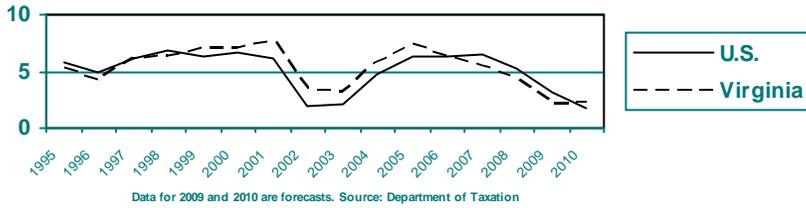


U.S. economic outlook bleak over the forecast horizon

The November forecast anticipates that tight credit conditions will result in a deeper downturn in housing and more cautious consumers which are expected to drag the U.S. economy into the longest and most severe recession since 1982. Highlights of the economic outlook for the next two years include:

- Real GDP is anticipated to decline by 0.4 percent in FY 2009 and increase only by a marginal 0.1 percent in FY 2010.
- National employment is expected to fall by 1.0 percent and 0.9 percent in FY 2009 and FY 2010, respectively.
- Job losses and tight credit conditions are expected to continue to curtail consumer spending.
- Inflation is expected to be in negative territory by the middle of 2009.
- The Federal Reserve is expected to continue trimming the federal funds rate, probably to 0.5%, although a zero rate is now possible.

Personal income growth to fall to recessionary rates



Extended economic downturn for Virginia

The Virginia economy is expected to be in recession over much of the forecast horizon. Most employment sectors will lose jobs over the next two years. The unemployment rate is expected to climb to 5.7% by FY 2010. Here is a look at what economists are predicting for Virginia:

- Personal income is expected to grow 2.1 percent in FY 2009 and 2.3 percent in FY 2010. Wages and salaries are expected to grow 2.6 percent in FY 2009 and 3.2 percent in FY 2010.
- Employment in the professional and business services sector is forecast to grow at 2.2 percent in FY 2009 and fall by 1.5 percent in FY 2010.
- Construction employment is expected to decline as the housing market slumps, falling 3.5 percent in FY 2009 and 5.9 percent in FY 2010.